CLEVELAND PUBLIC LIBRARY
BUSINESS INF. BUR.
CORPORATION FILE

1963

ANNUAL REPORT

GRAY
DRUG STORES, INC.

BOARD OF DIRECTORS

HAROLD C. BROWN	President, The Harold C. Brown Company
LLOYD C. DOUGLASS	Vice-President, Gray Drug Stores, Inc.
CARLYLE W. EVANS	President, Gray Drug Stores, Inc.
HENRY H. GRAY	Vice-President, Gray Drug Stores, Inc.
C. BERT McDONALD	Partner, McDonald & Company
GEORGE F. PRYOR	Personal Investments
JOHN W. REAVIS	Partner, Jones, Day, Cockley & Reavis
ADOLPH WEINBERGER	Chairman of the Board, Gray Drug Stores, Inc.
CARL WEINBERGER	Buyer, Gray Drug Stores, Inc.
JEROME WEINBERGER	Vice-President, Gray Drug Stores, Inc.

OFFICERS

ADOLPH WEINBERGER	Chairman of the Board
CARLYLE W. EVANS	President
LLOYD C. DOUGLASS	Vice-President
HERBERT H. DURR	Vice-President
HENRY H. GRAY	Vice-President
MARVIN L. KAHN	Vice-President
JEROME WEINBERGER	Vice-President
LOUIS BERWITT	Secretary
ROBERT E. BREIG	Treasurer
JOSEPH VALINS	Assistant Secretary
KENNETH FREY	Assistant Treasurer
I. ROSEN	President, Superior Laboratories, Inc.

TRANSFER AGENT AND REGISTRAR

THE CLEVELAND TRUST COMPANY — Cleveland, Ohio

AUDITORS

ERNST & ERNST — Cleveland, Ohio

COUNSEL

JONES, DAY, COCKLEY and REAVIS — Cleveland, Ohio

STOCK LISTED

MIDWEST STOCK EXCHANGE — Chicago, Illinois

HIGHLIGHTS OF OPERATIONS

FISCAL YEARS ENDED JUNE 30	1963	1962
Net Sales	$51,875,334	$44,952,417
Net Income	$ 662,366	$ 801,113
Net Income Per Share	$ 1.05	$ 1.27
Dividends Per Share	$ .80	$ .80
Working Capital	$11,692,984	$11,599,620
Current Ratio	3.08 to 1	3.37 to 1
Shareholders' Equity	$10,340,971	$10,182,328
Number of Regular Stores	109	109
Number of Discount Centers	43	25
Total Locations	152	134

Mr. Weinberger

Mr. Evans

LETTER TO SHAREHOLDERS

Net sales climbed to a record $51,875,334 during the year ended June 30, 1963, for an increase of 15.4 per cent over the $44,952,417 of the preceding year. Volume has doubled in just seven years.

Intense price competition affected profit margins throughout the past year. Profit before taxes was $1,399,066 or 2.71 per cent of net sales, compared with $1,611,213 or 3.58 per cent for the preceding year.

However, after deduction of taxes and all other charges, the Company earned net income of $662,366 or $1.05 a share on 629,654 shares outstanding as of June 30, compared with $801,113 or $1.27 a share in fiscal 1962.

Our financial condition remains very strong. Current assets of $17,325,758 are in a ratio of 3.08 to current liabilities. Net working capital climbed to $11,692,984, a new record.

Your Company had 152 units in operation at the fiscal year-end. Of these, 109 were conventional drug stores operated by our Gray Division, with all but one in Ohio and adjacent states.

Our King Division at the fiscal year-end was operating 32 drug departments located in discount department stores, and 11 discount drug stores. Of these 43 units, 22 are in Ohio. Other major areas of our discount drug activity are Florida and California, with 7 units each.

Five conventional drug stores were opened and five closed during the year. The King Division opened 23 discount units and closed five. King division sales were increased by $7,909,529 during the past year, due to the large number of new units opened; while conventional store sales declined 2 per cent, principally because of decreases in the central and southern Ohio markets.

The number of competitive drug outlets increased considerably in our market area during the past year. Competition included not only drug stores, but complete drug departments in supermarkets, discount department stores, and conventional department stores. Retail prices became more competitive as the number of outlets increased, and this is the primary cause for our drop in profits during the year.

Of course, the present competitive period was anticipated by Gray Drug in establishing its present large discount operation two years ago. The substantial additional volume, even at low profit margins, has been helpful in enabling us to maintain earnings at higher levels than would otherwise have been possible.

To meet today's competitive conditions, Gray Drug is changing its merchandising emphasis. Prescription departments, quality cosmetic lines, and sundry merchandise are being featured. We have also put into operation an aggressive, expanded advertising program featuring fast-moving products at very competitive prices. Results to date of the changes in our merchandising program have been encouraging.

For the current fiscal year, our present plans call for the opening of 6 Gray Division conventional drug stores and 11 King Division discount units. It is expected that a number of marginal units of both divisions will be closed or sold.

As a result of the many programs under way to build profits as well as sales, we are hopeful for higher earnings during the fiscal year now under way. Gray Drug has experienced many periods of unusual competition, and as a result of background and financial strength, has come through them with renewed vigor and improved earnings. We anticipate that the same historic trend will make itself felt in the future as it has in the past.

During the fiscal year just ended, your Company continued the quarterly dividend of 20 cents a share, thus marking 35 years of consecutive dividend payments.

Two new Directors were elected in September, 1962. They were Harold C. Brown, president of The Harold C. Brown Company, security dealers in Buffalo, N. Y., and C. Bert McDonald, managing partner of McDonald & Company, security dealers of Cleveland. Both Mr. Brown and Mr. McDonald, as well as our other directors, have shown great interest in the Company's operation, and their counsel is of valuable assistance to management.

Gray Drug now is doing business at an annual rate which would approximate $55,000,000 if continued for a full year. We are larger than ever before, stronger financially, and still growing rapidly, with prime store locations and a large, experienced organization capable of meeting all challenges in the retail drug field and in modern merchandising.

Sincerely,

Adolph Weinberger

Adolph Weinberger, Chairman

Carlyle W. Evans, President

SEPTEMBER 11, 1963

CONSOLIDATED BALANCE SHEET

GRAY DRUG STORES, INC. AND SUBSIDIARIES

ASSETS

	June 30, 1963	June 30, 1962
CURRENT ASSETS		
Cash	$ 1,945,073	$ 1,008,845
United States Treasury Bills — at cost plus accrued interest	2,730,560	3,471,080
Accounts receivable, less allowance of $30,000	483,152	384,287
Inventories, priced generally on the basis of the lower of cost (latest) or replacement market	11,792,695	11,192,605
Prepaid expenses	374,278	427,173
TOTAL CURRENT ASSETS	$17,325,758	$16,483,990
OTHER ASSETS	99,035	125,994
FIXED ASSETS — on the basis of cost		
Furniture, fixtures, and equipment	$ 4,353,377	$ 3,987,257
Leasehold improvements	2,481,189	2,430,247
	$ 6,834,566	$ 6,417,504
Less allowances for depreciation and amortization	3,203,325	2,886,449
	$ 3,631,241	$ 3,531,055
DEFERRED DEBENTURE EXPENSE	147,711	155,659
	$21,203,745	$20,296,698

ACCOUNTANTS' REPORT

Board of Directors
Gray Drug Stores, Inc.
Cleveland, Ohio

We have examined the consolidated balance sheet of Gray Drug Stores, Inc. and subsidiaries as of June 30, 1963, and the related statement of consolidated income and earnings retained for use in the business for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the accompanying balance sheet and statement of income and earnings retained for use in the business present fairly the consolidated financial position of Gray Drug Stores, Inc. and subsidiaries at June 30, 1963, and the consolidated results of their operations for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Cleveland, Ohio
August 21, 1963

Ernst, Ernst

LIABILITIES AND SHAREHOLDERS' EQUITY

	June 30, 1963	June 30, 1962
CURRENT LIABILITIES		
Trade accounts	$ 2,743,830	$ 2,241,368
Other liabilities and accrued expenses	1,722,313	1,592,711
Taxes other than federal taxes on income	292,305	261,930
Federal taxes on income — estimated	874,326	788,361
TOTAL CURRENT LIABILITIES	$ 5,632,774	$ 4,884,370
5% CONVERTIBLE SUBORDINATED DEBENTURES DUE 1982 — Note A	5,230,000	5,230,000
SHAREHOLDERS' EQUITY		
Common Stock, par value $1 a share — Notes A and B:		
Authorized 1,000,000 shares		
Outstanding 629,654 shares	$ 629,654	$ 629,654
Capital in excess of par value	3,889,783	3,889,783
Earnings retained for use in the business — Note A	5,821,534	5,662,891
TOTAL SHAREHOLDERS' EQUITY	$10,340,971	$10,182,328
LONG-TERM LEASE COMMITMENTS — Note D		
	$21,203,745	$20,296,698

See notes to financial statements.

STATEMENT OF CONSOLIDATED INCOME AND EARNINGS RETAINED FOR USE IN THE BUSINESS

GRAY DRUG STORES, INC. AND SUBSIDIARIES

	Year Ended June 30,	
	1963	1962
Net sales	$51,875,334	$44,952,417
Other operating income	153,801	143,152
Other income	55,241	25,921
	$52,084,376	$45,121,490
Costs and expenses:		
Cost of goods sold	$34,656,991	$29,267,905
Selling, general, and administrative expenses	15,007,100	13,451,891
Depreciation and amortization	758,985	667,295
Interest expense	262,234	123,186
	$50,685,310	$43,510,277
INCOME BEFORE FEDERAL TAXES ON INCOME	$ 1,399,066	$ 1,611,213
Federal taxes on income — estimated	736,700	810,100
NET INCOME	$ 662,366	$ 801,113
Earnings retained for use in the business at beginning of year	5,662,891	5,338,113
	$ 6,325,257	$ 6,139,226
Cash dividends declared — $.80 a share — Note C	503,723	476,335
EARNINGS RETAINED FOR USE IN THE BUSINESS AT END OF YEAR	$ 5,821,534	$ 5,662,891

See notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

Note A — 5% Convertible Subordinated Debentures:

The Indenture under which the Debentures were issued provides for sinking fund payments on or before January 25 in each year commencing in 1967, in an amount sufficient to redeem $285,000 principal amount of Debentures on the next ensuing February 1.

The Debentures are convertible into shares of Common Stock of the Company, at the option of the holder, at any time on or before February 1, 1982, at a conversion price (subject to adjustment in certain events) of $26 per share until February 1, 1967, $27 per share until February 1, 1972, and $28 per share thereafter until maturity.

At June 30, 1963, 201,154 shares of Common Stock were reserved for conversion of the Debentures.

Under terms of the Indenture, earnings retained for use in the business in the amount of $1,516,663 at June 30, 1963 were available for distribution to shareholders.

Note B — Stock Options:

Stock options were granted on April 29, 1960, to certain officers and key employees to purchase 18,000 shares of Common Stock of the Company. The price at which the options were granted was the approximate quoted market price ($15.83) at the date of grant except that the option price to the principal shareholder and two employees related to him was 110% of such price ($17.42) to permit qualification as a restricted stock option. All the options became exercisable on April 29, 1962, and expire on April 29, 1965. During the year ended June 30, 1963, no options were exercised, and at June 30, 1963, options for 15,900 shares were outstanding.

Note C — Dividends:

The Company deposited funds with the dividend disbursing agent on June 28, 1963, for payment of the dividend payable July 1, 1963.

Note D — Long-Term Lease Commitments:

The companies are lessees under a number of leases extending from one to twenty years. The annual aggregate minimum rental payable under such leases (many of which provide for additional rental if amounts based on specific percentages of sales exceed the minimum) amounted to approximately $1,975,000 at June 30, 1963.

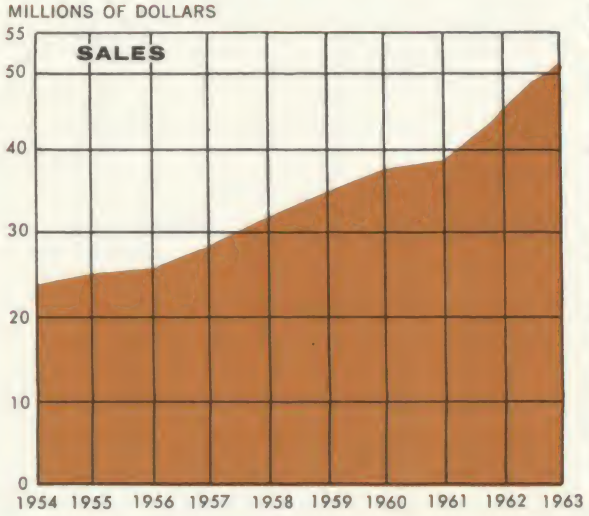
Note E — Pension Plan:

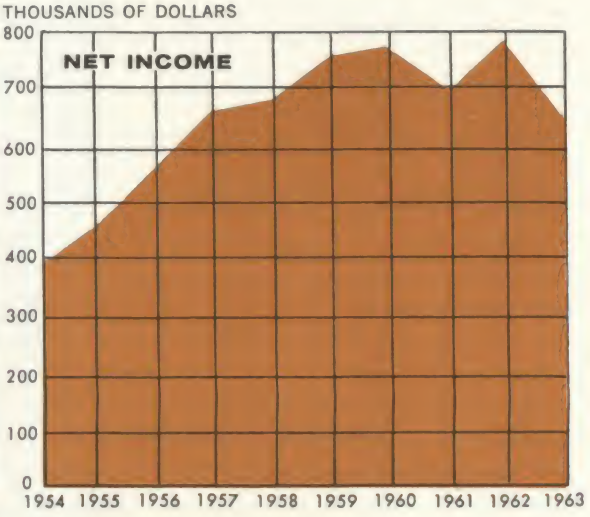
Contributions under the pension plan for employees of the companies amounted to approximately $157,000 for the year ended June 30, 1963, including amortization of the cost of past service benefits to retirement age of participants. The unfunded cost of past service benefits at June 30, 1963, was approximately $13,000.

Note F — Investment Tax Credit:

The investment tax credit (not material in amount) has been deferred and will be taken into income over the useful lives of the related assets.

10 years of progress





	1963	1962	1961	1960	1959	1958	1957	1956	1955	1954
Net Sales	$51,875,334	$44,952,417	$39,626,661	$37,552,700	$35,991,537	$32,249,706	$29,333,474	$25,543,059	$23,390,391	$22,578,421
Net Income Before Federal Taxes on Income	$ 1,399,066	$ 1,611,213	$ 1,467,793	$ 1,673,989	$ 1,607,591	$ 1,371,322	$ 1,404,880	$ 1,206,429	$ 953,560	$ 875,643
Net Income	$ 662,366	$ 801,113	$ 707,793	$ 793,989	$ 768,591	$ 692,322	$ 690,880	$ 576,429	$ 470,560	$ 407,643
Income per Common Share (1)	$ 1.05	$ 1.27	$ 1.42	$ 1.63	$ 1.58	$ 1.48	$ 1.47	$ 1.31	$ 1.07	$ .95
Income as a Percentage of Sales	1.28%	1.78%	1.78%	2.12%	2.14%	2.15%	2.36%	2.25%	2.01%	1.81%
Income as a Percentage of Shareholders Equity	6.41%	7.87%	9.04%	10.82%	11.20%	11.06%	11.95%	11.20%	9.94%	9.36%
Cash Dividends Declared — Common Stock	$ 503,723	$ 476,335	$ 393,062	$ 323,850	$ 256,720	$ 218,718	$ 208,928	$ 161,618	$ 145,893	$ 142,925
Dividends Per Share (1)	$ .80	$ .80	$ .80	$ .66⅔	$ .53⅓	$ .46⅔	$ .46⅔	$ .36⅔	$ .33⅓	$ .33⅓
Number of Shares Issued (1)	$ 629,654	$ 629,654	496,762	485,775	485,775	469,242	468,492	440,775	440,775	429,600
Net Working Capital	$11,692,984	$11,599,620	$ 6,218,365	$ 6,087,245	$ 5,630,703	$ 3,691,958	$ 3,509,318	$ 3,389,227	$ 3,014,120	$ 2,733,670
Total Assets	$21,203,745	$20,296,698	$14,195,991	$14,114,536	$13,262,079	$11,195,293	$ 9,883,411	$ 9,069,108	$ 8,279,362	$ 7,846,751
Long Term Debt	$ 5,230,000	$ 5,230,000	$ 2,139,200	$ 2,313,500	$ 2,313,500	$ 531,426	$ 576,377	$ 758,554	$ 917,839	$ 1,055,951
Shareholders Equity (2)	$10,340,971	$10,182,328	$ 7,826,699	$ 7,338,099	$ 6,867,960	$ 6,259,195	$ 5,781,497	$ 5,146,538	$ 4,731,727	$ 4,355,673
Book Value per Share (1)	$ 16.42	$ 16.17	$ 15.76	$ 15.11	$ 14.14	$ 13.34	$ 12.34	$ 11.68	$ 10.74	$ 10.14
Fixture and Leasehold Additions	$ 923,337	$ 713,221	$ 901,411	$ 748,758	$ 985,427	$ 903,700	$ 786,314	$ 467,887	$ 459,809	$ 452,272
Depreciation	$ 758,985	$ 667,295	$ 663,750	$ 633,483	$ 575,139	$ 507,717	$ 465,372	$ 451,573	$ 412,190	$ 383,368
Units in Operation — End of Year	152	134	117	111	107	102	86	81	78	80

GRAY
DRUG STORES, INC.